client briefing

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Clements
CHARTERED ACCOUNTANTS
(Incorporating J. F. Miller & Co.)

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Problematic expenses

The recent employee expenses report by GlobalExpense shows how both legitimate and illegitimate expenses claims can be costly for employers.

Legitimate claims

Around £124 million in VAT was unclaimed last year because businesses did not have valid receipts for a staggering 41% of employee mileage claims.

VAT can be recovered where employees are reimbursed for fuel used on business journeys – reimbursement can either be for the actual cost or as a mileage allowance. The fuel element of a mileage allowance may be based on HM Revenue & Customs' (HMRC) advisory fuel rates or on rates set by a motoring agency like the RAC or AA.

To recover VAT, it is necessary to obtain VAT invoices when employees purchase fuel, although these can be simplified invoices. Employees do not have to obtain an invoice for every purchase (although it is good practice to do so), as there just has to be sufficient fuel purchased to cover the amount of VAT reclaimed. HMRC recognises that the invoice amount may not match what is being reclaimed, although an invoice cannot be dated later than the period covered by a claim. So what can employers do?

- Make sure that employees are aware of the need to obtain receipts – and that a credit or debit card receipt will often be insufficient.
- Consider providing employees with one of the many different fuel cards that are available. One VAT invoice per month will then make the recovery of VAT much easier.

Illegitimate claims

Last year businesses lost more than £300 million through fraudulent employee expenses claims, and another £1 billion worth of claims were not compliant with company policy. The main reasons given for exaggerating claims were because employees felt underpaid, were not paid for overtime, or did not receive full reimbursement for costs they had incurred.

Here are a few suggestions:

- Have a clear written expenses policy that is accessible to employees. Less than half of employers do this, so it is not surprising that some 10% of all approved claims are not within company policy.
- Make sure that managers and directors who approve expenses get appropriate training and support. Most expenses claims are not queried or rejected.
- Expenses claims that are filed and dealt with promptly cut down on the risk of fraudulent claims from disgruntled employees.
- Insist on a receipt to support all claims.
- Consider using expenses management software because the cost of processing expenses can be huge compared with the amounts involved. The Forestry Commission reduced its processing costs by 60% after moving from a paper based system.

A change on entertainment

Following a recent judgment by the European Court of Justice, HMRC now accepts that VAT can be recovered on the cost of entertaining overseas customers. The law has been amended from 1 May, and backdated claims can be made subject to the normal four-year time limit.

Another tax amnesty in the pipeline

Tax amnesties offer a quick and cost-efficient way for the government to raise revenue. The first amnesty raised some £400 million at a cost of around £6 million.

Subsequently, there has been the New Disclosure Opportunity (NDO), the Liechtenstein Disclosure Facility (aimed at people with accounts or other assets held in Liechtenstein) and the Tax Health Plan (aimed at medical professionals).

Now we have the Plumbers Tax Safe Plan (PTSP), focused on people working in the plumbing, heating and gas installation trades. However, unlike some previous initiatives, the PTSP is actually open to anybody who wishes to bring their tax affairs up to date.

It is interesting that HM Revenue & Customs (HMRC) has also said that people not wanting to use the PTSP can voluntarily put their tax affairs in order and expect very similar terms to those offered by the plan, provided that they follow the guidelines.

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People have until 31 May to notify HMRC of an intention to disclose, and disclosure must then be made by 31 August. The attraction is the usual reduction in penalties but, unlike previous tax amnesties, the penalty depends on the behaviour that led to the underpayment.

For careless behaviour, no penalty at all will be due for 2008/09 and 2009/10. The number of years of disclosure also depends on behaviour, although HMRC expects most people to have to pay for a maximum of six years.

The Liechtenstein Disclosure Facility remains available until 31 March 2015, and for some people this might be the more favourable disclosure route.

For those taxpayers who have still not disclosed their overseas income and gains, the penalties may now be substantially higher. Since 6 April, the amount of penalty has depended on the category of the country in which the income or gains arise.

There is no change in respect of category 1 countries (those that automatically exchange information with the UK on savings income), but penalties are 150% of the normal amount for category 2 countries (information is exchanged but not automatically) and double for category 3 countries (no exchange of information).

Please get in touch if you wish to discuss options regarding undisclosed income. Given the possible routes currently available, the choice is not an easy one.

Picking up the tab...

The first raft of measures restricting tax credit eligibility for higher income households has just come into effect, with further changes due next April. Changes that came into effect on 6 April include:

- The rate at which your tax credits are reduced where income exceeds £6,420 has increased from 39% to 41%.
- The £545 family element of child tax credit is withdrawn where income exceeds £40,000 rather than £50,000, and the withdrawal rate is 41% instead of 6.67%.
- The weekly maximums for childcare are unchanged, but the claimable proportion is reduced from 80% to 70%.
- The amount of income disregard has been reduced from £25,000 to £10,000. Claims are initially based on income for the previous tax year, and the disregard is the amount by which current year income can rise before a claim is revised.

Take a couple with two children, both employed full-time, income of £45,000 and weekly childcare costs of £300. For 2010/11 they would have received tax credits of £7,179, but this year they will get about £1,800 less. Their marginal tax rate is probably 73% – income tax at 20%, national insurance contributions (NICs) of 12% and a 41% clawback of tax credits. In such a position, you might feel that a pay rise gives little benefit, since you will only keep 27p for each extra £1. If available, additional holiday entitlement or shorter working hours might be preferred.

Income is after deducting pension contributions and gift aid donations, so the government will pick up 61% of the tab (there is no NICs saving) if these are paid. If you are self-employed you could, for example, treat yourself to a business laptop, and save an additional 9% NICs – effectively funding just 30% of the cost yourself.

Sometimes the government might cover the full cost. The income reduction can also preserve tax credits for the following year, adding another 41% of tax saving – a total of 102% or 111%. And if you are a higher rate taxpayer the savings can be even greater.

Be warned though that this is a complex area, and unforeseen changes to your circumstances can easily ruin any tax planning. Contact us for further advice.

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Will you still need me?

The Beatles were singing about reaching 64, but since 6 April there is no choice – you can no longer require someone to retire when they reach 65. Many businesses already operate without a fixed retirement age, so they will have a relatively easy transition. But for others, there may be many questions:

How many employees will postpone retirement? Research suggests that nearly two-thirds of employees will postpone retirement, often because they have made insufficient pension provision.

What about pensions? Employees can claim the state pension and continue to work, or alternatively defer their pension in return for future enhanced benefits. You should consider reviewing the terms of any workplace pension scheme to support flexible later retirement.

Should I offer flexible working? Claiming the state pension and opting for flexible, part-time, working will be a popular option for many employees. However, be careful of discrimination if flexible working is offered to older workers and not to others.

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What can I do about an older worker who is underperforming? The only way you can remove an underperforming worker is by using the fair dismissal procedures that apply to all employees.

Can I have an employer-justified retirement age? Yes, but only in exceptional circumstances where such an age can be objectively justified – and this may be a difficult test to pass. To date, such retirement ages have mainly been used to retire people under 65, such as where a job requires a significant level of physical fitness.

Should I change my health and safety procedures? No. Many employers report that older workers have fewer accidents.

Do I have to have retirement discussions with my employees? There is no requirement to do this but you may find it helpful. Be careful of discriminating by singling out just older workers for discussions.

What about employee insurance and benefits? Group risk insured benefits such as income protection, life assurance, private medical cover and sickness insurance can cease when an employee reaches 65 (or the state pension age if higher), but not other benefits such as employee share schemes.

Where can I get more information? The Advisory, Conciliation and Arbitration Service (ACAS) and the Department for Work and Pensions websites have a range of relevant publications: www.acas.org.uk and www.dwp.gov.uk/age-positive

What the Budget sprang

Mr Osborne's second Budget managed to produce a few surprises, in spite of all the changes his first Budget contained.

There was an expectation among some commentators that George Osborne's second Budget would be a dull affair, as he had set the course for the next five years in his June 2010 'emergency' Budget. However, there were still a few unexpected announcements, alongside results from the many consultations launched last year.

Income tax The personal allowance rose by £1,000 for 2011/12, to £7,475. The Chancellor promised a smaller rise of £630 next tax year, based on his Budget inflation assumptions. However, the increase in the personal allowance will be matched by a reduction of the same amount in the basic rate limit, so the starting point for higher rate tax will remain unchanged. This follows on from the 2011/12 cut of £1,400 in the 40% tax starting point.

Indexation of taxes From 2012/13, increases to allowances and bands for direct taxes (eg income tax and inheritance tax) will generally be made in line with the consumer prices index (CPI) rather than the retail prices index (RPI). There will be several exceptions, notably to age-related income tax allowances, but the overall effect is a subtle increase in tax because allowances and bands will probably rise more slowly in the future. For example, over the last ten years to March 2011, the RPI rose by 35.0%, against 26.4% for the CPI.

Company car tax There was a general company car tax increase for 2011/12, following on from a rise in 2010/11. Alistair Darling announced planned 2012/13 increases in his December 2009 Pre-Budget Report and Mr Osborne did not alter those plans, instead revealing yet another tax rise, this time taking effect in 2013/14.

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Entrepreneurs' relief The lifetime limit for entrepreneurs' relief was doubled to £10 million, with effect from 6 April 2011. Gains up to the limit are taxed at 10%, rather than 18% or 28%. Only a few highly successful entrepreneurs are likely to benefit.

If you sense that the Chancellor was giving nothing away, you may be right. The state of the Government's finances is such that Mr Osborne has no scope for largesse and is still looking for ways of extracting extra revenue. To save tax, you need to look to your own financial plans, not the Chancellor's.

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Time to incorporate?

Changes to tax rates in April 2011 have increased the attraction for small businesses of trading as a limited company compared with self-employment, provided the owner draws income mainly as dividends.

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The corporation tax rate for small companies fell by 1% to 20% in April, equal to the basic rate of income tax. At the same time, the main rate of national insurance for self-employed individuals increased to 9%, with 2% on profits above £42,475.

The new rates mean that self-employed people with profits of £60,000 could save over £4,400 by incorporating the business. To gain maximum benefit they would have to take a salary of up to £7,475 (the personal allowance) and draw further income as dividends. The saving results from avoiding national insurance contributions and from the lower rates of income tax on dividends compared with earnings. More money can be saved at higher profit levels and by not drawing all the profit.

However, winding up a company is set to become more expensive. Normally, shareholders pay income tax of up to 42.5% on dividends. The exception is distributions in a liquidation, which are liable to capital gains tax (CGT), generally at 10%. At present, an extra statutory concession allows you to avoid the costs of a formal company liquidation and still pay CGT on distributions before the company's dissolution. However, draft legislation would impose a £4,000 limit on such distributions. No date has been set for the change.

If you are looking for investment into your business, changes announced in the March 2011 Budget may make it easier to find. The rate of income tax relief for investment under the enterprise investment scheme (EIS) increased from 20% to 30% from 6 April 2011. Further changes to the EIS rules next year will mean more companies will qualify.

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